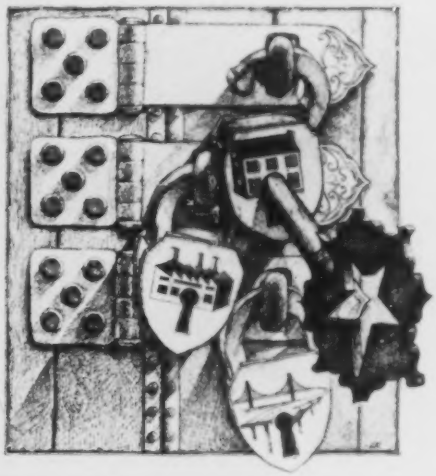
1983 Dodge/Sweet's Construction Outlook

Second Update
July 1983



The second quarter of 1983 marked the first anniversary of the construction industry's turnaround.

After four consecutive quarters of improvement, the building business was in a curious state of contrast at mid-1983. The broad measures of the market's performance were very encouraging:

- The Dodge Index of total construction contract value (the market's leading indicator) hit 148 in May—a new high.
- The value of construction put in place (the measure of ongoing work) reached $250 billion in the second quarter—another record breaker.

If things are that good, why isn't everybody happier? As usual, there is another side to the statistics:

- Unemployment in the building trades, at 20 percent in May, was still uncomfortably close to its 1982 high.
- Contractor failures continued to rise through the first half of 1983.
- Shipments of building materials, at a rate of $150 billion in the second quarter, were perking up. But profits of building products manufacturing firms weren't.

Clearly, the market is heading in the right direction. But recovery hasn't developed far enough to deliver tangible results in the places where they count most. At least not yet.

Keeping A Good Thing Go[illegible]

So far, this has been a housing recovery, and not much more. Experience shows, however, that wherever the construction industry is going, housing gets there first. So if the current rise in homebuilding can be sustained, nonresidential construction will eventually catch up, as it usually does.

Several conditions must be met, however, to nudge the year-old recovery into its second phase of expansion:

- Interest rates must decline further if the housing market is to top its present 1.6 million unit plateau.
- Public spending—both Federal and local—must be unlocked to reverse the declining trend of public works construction.
- The economy's recovery must accelerate to take up excess capacity and prepare the way for a turnaround of commercial and industrial building.

Chances are excellent that all of these conditions will be met during the next year or two.

Mortgages and Housing

The reappointment of Paul Volcker to head the Federal Reserve removed one element of uncertainty about monetary policy. Mr. Volcker may not be the building industry's first choice—or its second, either. But with the Fed committed to monetarism, a pragmatic monetarist like Volcker is to be preferred over a dogmatic monetarist.

As long as economic recovery holds a higher priority than inflation in national policy—as it must for the balance of 1983 and through 1984—even a monetarist central banker will lean toward credit ease. This puts the focus of interest rates less on the supply of credit where it has been until recently, and more on the demand for it.

It would be hard to make a case for "crowding out" during the next year and a half. Business demand for capital funds, according to current plans for investment in plant and equipment, will remain light for the time being. Federal government borrowing, which has dominated the money market recently, will continue to be huge, but no larger than it is now. As the economy continues to

make its way from deep recession through the early stages of recovery, a limited demand for funds, coupled with an adequate supply, means there will be ample credit to go around. This leaves room for a further modest decline of long-term rates. The housing outlook which follows is based on the assumption that mortgage rates (25 year conventional 75 percent loan) will continue to recede slowly from their recent (1983:I) level of 13½ percent to a low of 12¼ percent by mid-1984, and rise gently thereafter. This means that there is potential for additional expansion of homebuilding over the next year or two. But it also means that the ceiling is not far beyond 1983's volume.

As mortgage rates drift slowly downward over the next several quarters, housing starts are expected to fluctuate in the range of 1.60 to 1.65 million during the second half of 1983, and then creep up to a rate of 1.75 million by the closing quarter of 1984. On a calendar year basis, this quarterly pattern would yield a full year total of 1,585,000 units in 1983 and 1,685,000 in 1984. In both years, the gains in one-family homes will exceed those of multifamily units.

Public Spending and Nonbuilding Construction

Like monetary policy, public spending—at least for public works construction—has changed course abruptly, from restraint to stimulus. And like lower interest rates, the loosening of the Federal purse strings adds another dimension to the construction outlook that has been missing for several years.

The steady decline of public works construction since 1979 is being reversed, if only temporarily, by a pair of very recent legislative acts. They are reviving the tradition of using public works spending as a stimulus to the economy in times of high unemployment. The Surface Transportation Assistance Act (with its 5¢ fuel tax) and the Emergency Supplemental Appropriations Act (better known as the Public Works Jobs Bill) are just now beginning to make their influence felt on contracting for new construction.

The Surface Transportation Assistance Act is by far the more consequential of the two new programs, both in its duration and the dollars it will generate. The Public Works Jobs Bill will merely shift a few billion dollars of future appropriations for already existing programs into the current fiscal year, leaving a comparable gap in fiscal year 1984 (or 1985). The fuel tax, on the other hand, will divert as much as $5½ billion annually from the private sector to public works construction through the end of fiscal year 1986—a potential windfall of $20 billion or more.

In 1983, contracting for public works construction is now estimated at $28.7 billion, up 11 percent from last year's total. Highway and bridge construction, at an estimated $15.1 billion, will be 23 percent higher in 1983.

Utility construction cancellations have been outnumbering new plans. With 6 projects started in 1983's first half, and only another 4 or 5 scheduled to start before year-end, the 1983 forecast of

1983 National Estimates Dodge Construction Potentials

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		1982 Actual	1983 Forecast	Percent Change 1983/82
Nonresidential Buildings				
Floor Area (millions of square feet)	Office Buildings	259	236	− 9
	Stores & Other Commercial	306	345	+13
	Manufacturing Buildings	116	90	−22
	Total Commercial & Manufacturing	681	671	− 1
	Educational	74	70	− 5
	Hospital & Health	70	73	+ 4
	Other Nonresidential Buildings	112	125	+12
	Total Institutional & Other	256	268	+ 5
	Total Nonresidential Buildings	937	939	—
Contract Value (millions of dollars)	Office Buildings	$ 17,333	$ 16,875	− 3
	Stores & Other Commercial	10,794	13,225	+23
	Manufacturing Buildings	9,361	5,175	−45
	Total Commercial & Manufacturing	$ 37,488	$ 35,275	− 6
	Educational	$ 6,142	$ 5,875	− 4
	Hospital & Health	7,833	8,350	+ 7
	Other Nonresidential Buildings	7,914	9,075	+15
	Total Institutional & Other	$ 21,889	$ 23,300	+ 6
	Total Nonresidential Buildings	$ 59,377	$ 58,575	− 1
Residential Buildings				
Dwelling Units** (thousands of units)	One-Family Houses	636	1,000	+57
	Multifamily Housing	434	585	+35
	Total Housekeeping Residential	1,070	1,585	+48
Floor Area (millions of square feet)	One-Family Houses	994	1,555	+56
	Multifamily Housing	426	575	+35
	Nonhousekeeping Residential	59	67	+14
	Total Residential Buildings	1,479	2,197	+49
Contract Value (millions of dollars)	One-Family Houses	$ 37,603	$ 61,975	+65
	Multifamily Housing	16,748	22,050	+32
	Nonhousekeeping Residential	4,243	4,800	+13
	Total Residential Buildings	$ 58,594	$ 88,825	+52
Nonbuilding Construction				
Contract Value (millions of dollars)	Highways & Bridges	$ 12,259	$ 15,100	+23
	Sewer & Water	7,347	7,175	− 2
	Other Public Works	6,260	6,400	+ 2
	Total Public Works	$ 25,866	$ 28,675	+11
	Utilities	$ 11,488	$ 9,500	−17
	Total Nonbuilding Construction	$ 37,354	$ 38,175	+ 2
All Construction				
Contract Value (millions of dollars)	Total Construction	$155,325	$185,575	+19
	Dodge Index (1977 = 100)	111	133	

**F.W. Dodge basis

1983 Regional Estimates
Dodge Construction Potentials

Second Update
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Northeast

Connecticut, District of Columbia, Delaware, Massachusetts, Maryland, Maine, New Hampshire, New Jersey, New York, Eastern Pennsylvania, Rhode Island, Virginia, Vermont

Contract Value (millions of dollars)	1982 Actual	1983 Forecast	Percent Change 83/82
Nonresidential Buildings			
Commercial and Manufacturing	$ 6,520	$ 7,325	+12
Institutional and Other	4,433	5,000	+13
Total	$10,953	$12,325	+13
Residential Buildings			
One-Family Houses	$ 5,717	$ 9,800	+71
Multifamily Housing	3,060	4,300	+41
Nonhousekeeping Residential	1,016	1,175	+16
Total	$ 9,793	$15,275	+56
Nonbuilding Construction			
Highways and Bridges	$ 2,463	$ 3,075	+25
Other Public Works	2,901	2,925	+ 1
Utilities	1,198	600	−50
Total	$ 6,562	$ 6,600	+ 1
Total Construction	$27,308	$34,200	+25

South

Alabama, Arkansas, Florida, Georgia, Southern Illinois, Kansas, Louisiana, Mississippi, Missouri, North Carolina, Nebraska, Oklahoma, South Carolina, Tennessee, Texas

Contract Value (millions of dollars)	1982 Actual	1983 Forecast	Percent Change 83/82
Nonresidential Buildings			
Commercial and Manufacturing	$14,327	$13,200	− 8
Institutional and Other	7,625	8,700	+14
Total	$21,952	$21,900	—
Residential Buildings			
One-Family Houses	$17,788	$27,550	+55
Multifamily Housing	7,257	9,675	+33
Nonhousekeeping Residential	1,656	1,725	+ 4
Total	$26,701	$38,950	+46
Nonbuilding Construction			
Highways and Bridges	$ 4,244	$ 5,125	+21
Other Public Works	4,630	4,725	+ 2
Utilities	3,207	3,500	+ 9
Total	$12,081	$13,350	+11
Total Construction	$60,734	$74,200	+22

Midwest

Northern Illinois, Indiana, Iowa, Kentucky, Michigan, Minnesota, North Dakota, Ohio, Western Pennsylvania, South Dakota, Wisconsin, West Virginia

Contract Value (millions of dollars)	1982 Actual	1983 Forecast	Percent Change 83/82
Nonresidential Buildings			
Commercial and Manufacturing	$ 7,371	$ 5,550	−25
Institutional & Other	4,827	4,500	− 7
Total	$12,198	$10,050	−18
Residential Buildings			
One-Family Houses	$ 5,374	$ 9,125	+70
Multifamily Housing	2,521	3,050	+21
Nonhousekeeping Residential	403	550	+36
Total	$ 8,298	$12,725	+53
Nonbuilding Construction			
Highways and Bridges	$ 3,021	$ 3,675	+22
Other Public Works	2,670	2,725	+ 2
Utilities	2,721	1,300	−52
Total	$ 8,412	$ 7,700	− 8
Total Construction	$28,908	$30,475	+ 5

West

Alaska, Arizona, California, Colorado, Hawaii, Idaho, Montana, Nevada, New Mexico, Oregon, Utah, Washington, Wyoming

Contract Value (millions of dollars)	1982 Actual	1983 Forecast	Percent Change 83/82
Nonresidential Buildings			
Commercial and Manufacturing	$ 9,270	$ 9,200	− 1
Institutional & Other	5,004	5,100	+ 2
Total	$14,274	$14,300	—
Residential Buildings			
One-Family Houses	$ 8,724	$15,500	+78
Multifamily Housing	3,910	5,025	+29
Nonhousekeeping Residential	1,168	1,350	+16
Total	$13,802	$21,875	+58
Nonbuilding Construction			
Highways and Bridges	$ 2,531	$ 3,225	+27
Other Public Works	3,406	3,200	− 6
Utilities	4,362	4,100	− 6
Total	$10,299	$10,525	+ 2
Total Construction	$38,375	$46,700	+22

utility construction contract value has shrunk to $9.5 billion, a 17 percent decline from 1982's total.

Capital Spending and Commercial/Industrial Building

The economy's turnaround in the opening quarter of 1983 was the first link in a chain of events leading to the recovery of commercial and industrial building. The quickening pace of business activity in the second quarter brought added support, but the expansion process has a long way to go before enough slack has been taken up to justify making net additions to the capital stock. For another couple of quarters, contracting for commercial and industrial building will remain at its cyclical low point (650 million square feet), motivated only by relocation, replacement, and upgrading —but *not* expansion.

Experience of the 1975 recession/recovery period shows what to expect next. Once recovery from the mid-1970's recession began, it took another four quarters before the first stirrings of contracting for commercial and industrial building appeared. Even then, recovery was hesitant at first. Considering

the greater severity of the early 1980's recession, it would be reasonable to look for the next expansion of commercial and industrial building to begin around the middle of 1984.

Three key categories of nonresidential building—stores, offices, and factories—are responsible for most of its volatility, and deserve special attention. These three sensitive building types are now heading in three different directions, a condition that is typical of a general nonresidential building turning point. Contracting for offices declined during 1983's first half and still has a long way to go before reaching the bottom of its cycle. Industrial building appears to have hit bottom, but is showing little inclination to recover. Retail building not only has bottomed out, but already has three quarters of recovery behind it.

Taken together, these offsetting cyclical movements within the nonresidential building market preclude any net improvement in total square footage of nonresidential building contracting in 1983. The stage is set, however, for a sustained recovery beginning in 1984.

Contracting for retail building is already leading the nonresidential sector out of its deep recession. The demand for stores and warehouses, which is motivated by consumer relocation, is derived from homebuilding. The year-old housing recovery began to stimulate retail building late in 1982. In 1983, the greatly improved housing market is bringing forth a modest but important 15 percent gain in contracting for stores and warehouses that will develop into a much stronger expansion in 1984, as retailers strive to catch up with the current year's wave of homebuilding.

Industrial construction will be the next key nonresidential building market to respond. However, excess capacity left over from the recession will be inhibiting new construction until mid-1984. Meanwhile, contracting is holding steady at 95 to 100 million square feet while rising industrial production gradually absorbs the surplus.

The office building market, which is coming off a boom of unprecedented proportions, is now glutted with space. To restore a workable balance between supply and demand will require several years of below-normal office building. (Normal is approximately 200 million square feet per year; current contracting is still up around 250 million, on the way down from 325.) It's unlikely that balance will be achieved before 1986. Until then, offices will be a drag on the nonresidential building recovery.

The sequence of the nonresidential building recovery is sending out two conflicting signals. One is that expansion has already taken hold in the retail building sector. The other is that a few nonresidential building types, offices in particular, will be slow to link up. This delay means that the recovery of the nonresidential building market won't hit full stride until well into 1985.

1983's Second Half: Plateau, Then Go

For the next couple of quarters, contracting for total new construction will stabilize, due to some temporary trade-offs:

- *Housing* will continue to advance, but not very much. Further expansion by an additional 50,000 units (annual rate) will boost contract value 5 percent higher during the second half. Against this...
- *Nonresidential building* will be about 7 percent lower in the second half. A lot of the weakness will be concentrated in office building. In addition...
- *Nonbuilding construction* will be off its first half pace by roughly 4 percent despite a higher level of public works construction. The reason: a reduced amount of utility contracting.

Expansion will resume during 1984, as the nonresidential building cycle reverses direction. Meanwhile, for 1983, *partial* recovery of construction markets to $185.6 billion of contract value means a solid gain of 19 percent, with the promise of more on its way.

Prepared by the Economics Department
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The Outlook

Nonresidential Building Contract Value

Seasonally adjusted annual rates, in billions of dollars

Year/Quarter		Total	Commercial/ Industrial	Institutional
1982	I	$66.5	$45.8	$20.7
	II	57.8	37.2	20.6
	III	58.2	35.5	22.7
	IV	55.0	31.5	23.5
1983	I	$61.6	$38.2	$23.4
	II	59.6	35.7	23.9
	III	57.8	34.7	23.1
	IV	55.3	32.5	22.8
1982		$59.4	$37.5	$21.9
1983		$58.6	$35.3	$23.3
% Change		– 1	– 6	+ 6

Residential Building Contract Value

Seasonally adjusted annual rates, in billions of dollars

Year/Quarter		Total	One Family	Multi-Family*
1982	I	$49.5	$32.0	$17.5
	II	54.2	33.6	20.6
	III	60.6	38.8	21.8
	IV	70.1	46.1	24.0
1983	I	$86.3	$59.2	$27.1
	II	86.8	59.4	27.4
	III	89.1	62.9	26.2
	IV	93.1	66.4	26.7
1982		$58.6	$37.6	$21.0
1983		$88.8	$62.0	$26.8
% Change		+52	+65	+28

*Includes Nonhousekeeping Residential Buildings

Nonbuilding Construction Contract Value

Seasonally adjusted annual rates, in billions of dollars

Year/Quarter		Total	Public Works	Utilities
1982	I	$42.1	$28.3	$13.8
	II	31.6	25.4	6.2
	III	34.4	25.3	9.1
	IV	41.3	24.5	16.8
1983	I	$30.4	$24.3	$ 6.1
	II	47.6	30.2	17.4
	III	37.2	30.2	7.0
	IV	37.5	30.0	7.5
1982		$37.4	$25.9	$11.5
1983		$38.2	$28.7	$ 9.5
% Change		+ 2	+11	–17